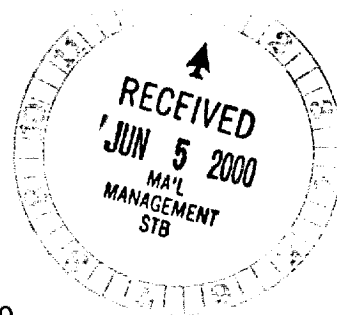


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June 5, 2000

HAND DELIVERY

Surface Transportation Board
Office of the Secretary
Case Control Unit
Attn: STB Ex Parte No. 582
1925 K Street, N.W.
Washington, DC 20423-0001

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Office of the Secretary

JUN 05 2000

Part of
Public Record

Re: Ex Parte No. 582 (Sub-No. 1), Major Rail
Consolidation Procedures

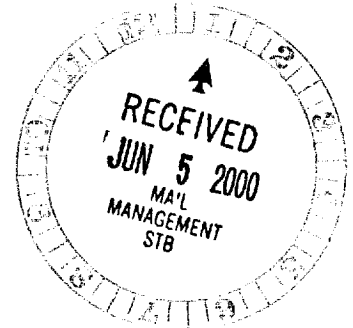
Dear Ladies/Gentlemen:

Enclosed please find an original and 25 copies of Reply Comments on Behalf of the Port Authority of New York and New Jersey in the above-captioned proceeding. In addition, please find a 3.5-inch IBM-compatible floppy diskette convertible into 7.0 WordPerfect of the same document.

Very truly yours,

Paul M. Donovan

BEFORE THE
SURFACE TRANSPORTATION BOARD



EX PARTE NO. 582 (Sub-No.1)
MAJOR RAIL CONSOLIDATION PROCEDURES

REPLY COMMENTS ON BEHALF OF THE
PORT AUTHORITY OF NEW YORK AND NEW JERSEY

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Attorneys for The Port Authority
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DATED: June 5, 2000

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Office of the Secretary

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Public Record

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB EX PARTE NO. 582 (Sub-No.1)
MAJOR RAIL CONSOLIDATION PROCEDURES

REPLY COMMENTS ON BEHALF OF THE
PORT AUTHORITY OF NEW YORK AND NEW JERSEY

INTRODUCTION

The Port Authority of New York and New Jersey ("the Port Authority") has reviewed the comments filed by the various parties in this proceeding, and several observations. First, with notable exceptions, there appears to be considerable support for altering the Board's merger procedures to more adequately reflect today's, rather than yesterday's rail industry. Second, again with some notable exceptions, there seems to be a recognition that recent mergers have generally had a negative impact upon the rail industry's ability to serve the public. The Port Authority agrees with these majority views, and also believes that any future merger applications must be reviewed with the past, as well as the future, in mind.

The Port Authority will address various of the comments in turn:

The Association of American Railroad

The Association of American Railroads ("AAR") makes several important and largely irrefutable points. For example, AAR states that "[r]ailroading is an extraordinarily capital intensive business." (AAR Comments, p. 3) The AAR also properly contends that "[by] any relevant measure of profitability, the nation's railroads still lag far behind other industries." (AAR Comments, p.6) Most importantly, the AAR recognizes that new infrastructure spending is critical to further improvements in service and productivity.

The AAR concludes that since there is presently a lack of infrastructure, and a lack of capital to provide additional infrastructure, causing serious service problems, the Board should not use its merger procedures to provide additional competition for shippers and others relying upon rail service lest the additional competition reduce rail revenues. In other words, AAR repeats the often heard plea "protect our franchise monopoly or we will be unable to provide service."

In fact, the sorry financial state of the carriers serving New York/New Jersey--\$13 billion in long term debt, shrinking traffic bases from diversions to highway and other ports, and continuing infrastructure shortages with no prospect of capital investment to remedy those shortfalls--is not the result of regulation, reregulation or any other external force. It is the

result of a foolish bidding war between Norfolk Southern and CSX which led to a bonanza for Conrail investors and a substantial negative impact on the public interest, including the Port Authority's interests at New York/New Jersey.

As noted in our Comments herein, this was made virtually inevitable by the Board's inability to review the financial aspects of the transaction before it became a fait accompli. Instead of raising the specter of back door reregulation, the AAR would, in the Port Authority's opinion be better served by recognizing that the rail industry's own follies and merger excesses have created an unhealthy economic climate for the carriers.

Burlington Northern Santa Fe

The Burlington Northern Santa Fe ("BNSF") takes the position that the Board's concern that its proposed merger with the Canadian National ("CN") could trigger a consolidation of U.S. and Canadian railroads resulting in two transcontinental systems is not well founded. BNSF "does not believe that anyone can predict the future so conclusively...." (BNSF Comments, p. 14) In essence, BNSF would not have the Board assess the likely competitive responses of other railroads to mergers, but continue on, in effect, with the current one case at a time process.

The BNSF philosophy is probably best understood in the context of its argument at page 15 of its comments. BNSF contends:

Accordingly, BNSF recommends that the Board require merging railroads to supplement their applica-

tions if, by the date on which intervenor testimony is due, another combination has been announced and definitive merger documents publicly filed with the SEC. The supplement would specifically address whether (a) any new competitive problems would be created by the two mergers, and (b) any new service problems might result. However, the Board should not, under any circumstances, cure any problems created by the second-filed merger application by imposing conditions on the first-filed merger. (Footnote omitted, emphasis supplied.)

The quoted statement reflects two things. First, contrary to its assertion that no one can predict the response of other carriers to its anticipated merger application, BNSF fully expects its application to trigger a response, and is concerned that the response may result in conditions being placed on the BNSF/CN merger. Second, not surprisingly, BNSF is concerned with its private interests not the public interest.

Canadian National

In essence, the CN seeks to maintain the status quo with respect to the examination of downstream effects. While paying lip service to some minor revisions, it would maintain the case-by-case approach with respect to examining downstream transactions, "three-to-two" issues and public benefits claimed by the applicants.

CN's suggestions simply ignore the rail industry as it presently exists, and would have the Board pretend that its prior merger procedures can protect and promote the public interest even with a vastly different rail structure in place. The Port Authority strongly disagrees with this posture.

CSX

The Port Authority finds itself in substantial agreement

with several of the positions expressed by CSX. For example, the Port Authority agrees:

The Board should become even more proactive in combinations in the preauthorization stage, making greater in-depth examinations of areas closely related to service to shippers, including the integration process, the capital plans of the applicants, the capacity and capability of their proposed network, and "nuts-and-bolts" issues such as car supply. (CSX Comments, p. 7)

This statement closely parallels the comments filed by the Port Authority herein. The Port Authority has also called for greater Board involvement at the preauthorization stage to prevent consolidations from becoming financial fait accompli before the Board has an opportunity to examine the consequences of the transaction.

The Port Authority also agrees with CSX's suggestions that: "The Board must look more carefully at alternatives to full combinations, such as marketing alliances, line swaps, and other joint ventures...in the light of whether the same benefits could be obtained as a practical matter without a full combination."

The Port Authority agrees that integration plans should be looked at more closely in the future. CSX does not, however, recognize the major impediment to effective review of those plans. In past cases, faced with obvious operational problems inherent in their integration plans, applicants have adopted a "we know how to run our railroad better than you" attitude, and the Board has been willing to accept these assertions without substantial factual support. This must change.

As noted in its initial comments, the Port Authority strong-

ly recommends reform of the fact finding process in consolidation proceedings to allow an objective fact finder, likely an Administrative Law Judge or other qualified person, to hear the cross-examination of supporting witnesses, particularly when disputed operating plans or downstream effects issues are involved. It has become painfully clear that credibility is as much an issue the rail consolidation proceedings as it is in every other form of judicial and administrative action.

Perhaps the most important CSX comment with which the Port Authority agrees is that "mergers must work toward making the rail industry more efficient, increasing rail demand by improving service, and thus improving their capacity to raise capital." (CSX Comments, p. 8) The Port Authority would amend this statement slightly by providing that no merger should be approved unless it could be found to have those effects.

The Port Authority also believes that CSX is correct in stating that the Board should require any merger application involving wither of the two major Canadian railroads to include specified information regarding cross-border issues.

KANSAS CITY SOUTHERN

The Port Authority strongly supports the position stated by the Kansan City Southern Railway ("KCS") to the effect that the Board should "require that parties to any future merger proceeding examine the impact of their proposed transaction on the benefits to competition that they claimed in securing authority for prior mergers." While KCS is obviously focusing on the

impact a merger involving the BNSF and CN would have on its Alliance with the CN which was touted as a major benefit in the CN/IC merger, its reasoning applies with equal force to the carriers serving New York/New Jersey.

CSX and Norfolk Southern claimed that their acquisition of Conrail would benefit New York/New Jersey by providing for competitive rail service where a Conrail monopoly had existed. The competition provided by these carriers is not only with respect to each other. It also provides competition between CSX and NS at New York/New Jersey and CN serving Halifax insofar as export/import traffic is concerned. Any combination that involved CN and one of the carriers serving New York/New Jersey would, therefore, reduce the competitive benefits promised as a result of the Conrail transaction. Hence, the Board should examine that reduction in competition as a downstream effect of any proposed CN merger.

CONCLUSION

Union Pacific ("UP") "questions whether additional Class I consolidations will ever be in the public interest, even though mergers have provided important benefits in the past." The Port Authority takes this statement to mean that, at least at the present time, no projected Class I merger would be in the public interest. The Port Authority is inclined to agree.

As has been stated by several commenters, the current rail system is roughly balanced. Another round of mergers, resulting in two transcontinental railroads, would likely result in a

similar balance, but with fewer competitors. The Port Authority does not believe that such a round of mergers would produce additional capacity. This leads the Port Authority to ask: with little or no redundant capacity left in the rail system, what possible benefits would flow from a reduction in the number of competitors with no real increase in efficiency or service?

The Port Authority requests that the Board adopt those recommendations made in its initial comments and those put forward in this document.

Respectfully submitted,



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Attorney for The Port Authority of
New York and New Jersey

CERTIFICATE OF SERVICE

I hereby certify that I have this 5th day of June, 2000, caused the foregoing document to be served upon all parties of record in this proceeding by first class mail, postage prepaid.



Paul M. Donovan